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Bank Risk and National Governance in Asia

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Bank risk and national governance in Asia

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Research Question

Does national governance quality impact on bank risk?

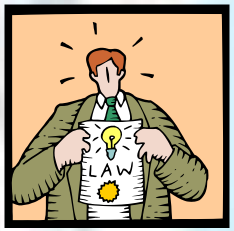
Background

Modelling bank risk has important policy implications post GFC.

The role that national governance plays in bank risk has not been previously considered.

What are the benefits?

- $ Adds governance variables to a traditional model of bank risk to see if governance has any role in determining bank risk.
- $ Uses interaction variables to see if national governance reinforces any risk reducing impact of conventional variables.
- $ Allows for the impact of economic cycles.
- $ Aids in determining the appropriate regulatory response to the GFC banking crisis.



Which countries and why?

- $ All ASEAN member nations plus Australia, Japan and New Zealand.
- $ Adds the last three countries to determine if developed versus developing nation status has any impact.
- $ Provides a longer run view of bank risk in a post crisis situation (after the Asian Financial Crisis).
- $ A longer run view helps inform the policy reforms that are occurring post GFC.

bankscope

What have I done?

- $ Data from 1997 to 2011.
- $ Governance measures from World Bank; Bank data from BankScope; economic data from IMF.
- $ Feasible GLS estimation to control for autocorrelation and heteroscedasticity.

The World Bank
Working for a World Free of Poverty

Research Design (the boring bit)

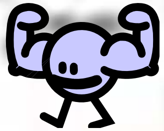
•Four measures of bank risk (revenue volatility *2, asset quality, distance to default)

•Controls for capital holding, franchise value, bank size, revenue composition and loan growth.

Results

$ Higher national governance results in lower bank level risk

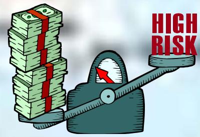
$ Improved national level governance reduces the negative aspects of "too big to fail"



$ Bank capital holding reduces bank risk, but only up to a point.

$ Once the critical point is reached, bank risk will start to increase.

$ National regulator quality can improve the effectiveness of bank capital in reducing bank risk.



$ Improved economic circumstances are associated with lower bank risk.

$ Rapid loan growth increases bank risk: If it grows too fast it's a weed.